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USDOC FOR ITS/TD/ENERGY DIVISION
TREASURY FOR IA (ALICE FAIBISHENKO)
DOE FOR INTERNATIONAL AFFAIRS KDEUTSCH AND ALOCKWOOD
STATE PASS TO USTR (EISSENSTAT/MELLE)
STATE PASS TO FEDERAL RESERVE (CARLOS ARTETA)
NSC FOR DAN FISK

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SUBJECT: MEXICO ECONOMIC NOTES, JUNE 22 - JULY 13

Summary

¶1. (SBU) The Calderon Administration is working with the Mexican Legislature to promote a fiscal reform initiative, possibly a prelude to a series of other reforms (energy, labor, education, etc.). Over the past two weeks, we have spoken with officials outside and inside the Congress to get a snapshot of the debate. The opposition Party of the Democratic Revolution (PRD) and Institutional Revolutionary Party (PRI) have voiced varying levels of concern about the proposed reform. Nevertheless, the PRI has indicated its willingness to work with the Calderon government to reach a compromise that would allow the fiscal reform to move forward. In a negative sign for prospects of reforms in education, the national teacher's union has effectively named their current leader, Elba Ester Gordillo, president-for-life. Under Gordillo's leadership, the National Education Workers Union, has consistently blocked attempts at reforming Mexico's corrupt and poorly reforming education system. The terrorist attack on gas pipelines in central Mexico forced several factories to halt production temporarily until alternate supplies could be arranged. Finally, Washington State Governor Christine Gregoire discussed apple tariffs and cross-border trucking with the Secretariat of the Economy.

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Labor Politician Opposes Fiscal Reform Initiative

¶2. (U) Although the PRI is willing to work with the Calderon administration to pass fiscal reform, the Coordinator of the "labor" faction within the party has reportedly expressed strong opposition to the initiative. According to a senior staffer, the labor faction Coordinator, Patricio Flores Sandoval, indicated that he will do everything within his

power to oppose the initiative. In addition to being a Federal Deputy, Flores Sandoval is also a member of the (Council of Mexican Workers') CTM's National Committee. The CTM is the largest labor federation in Mexico and is roughly equivalent to the AFL-CIO. Flores Sandoval's stance in opposition to the fiscal reform initiative is more hard line than that taken publicly by either the PRI or the CTM. However, he is an influential figure among PRI Federal Deputies and his opposition to the reform could become a focal point for other members of the national legislature who are against it.

Hacienda Official on Reform Calendar

13. (SBU) The head of Hacienda's Economic Planning Unit, Miguel Messmacher, told the Embassy and two visiting Treasury officials that Finance Secretary Carstens' reform priorities include fiscal reform, measures to deepen the financial system, infrastructure, and energy. Messmacher only spoke about fiscal reform in general terms and said that the government is talking about energy reform "in a basic way." He added that Hacienda wants to make Pemex more like a business, reform the company's fiscal regime, and improve corporate governance -- noting that the latter may come first. When asked about prospects for educational reform, he said that there will be talk about it, but that it will require a significant amount of work because of "political sensitivities" associated with dealing with the unions. He said that the window of opportunity for passing reforms that require significant political capital could be lost after April 2008 because the lower house of Congress would be gearing up for the 2009 elections. He believes the PRI will back some measures after this timeframe, but that securing their support will be more difficult.

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Energy Reform Debate Drifting

14. (SBU) Francisco Diaz Palafox (protect), lead PRI staffer on the Mexican Senate Energy committee was non-committal about whether the Senate would be able to propose and pass any kind of energy reform. He noted that early in the closed-door talks over limited energy reforms that would give Pemex some additional budget autonomy and freedom from restrictive government procurement rules, representatives from all three parties had agreed not to raise larger scale constitutional reform. Palafox added that within the past month, at least two National Action Party (PAN) Senators rejected the earlier no-constitutional amendment rule, and have poisoned the discussion.

New Tax Reform Law May Affect Maquilas

15. (U) Although Hacienda had previously said that the proposed fiscal reform package would not have a negative impact on maquilas, officials now acknowledge that it will. Representatives from the National Maquiladora Council (CNIME) met with Hacienda to discuss the effects of the reform. Maquila owners complain that they would be subject to double taxation, paying taxes in Mexico and in the U.S. where the parent company headquarters is located because the cost of inputs from the U.S would not be fully deductible under the new regime.

Gordillo Now "President for Life"

16. (SBU) During an "extraordinary" meeting of the National Education Workers Union's (SNTE) Political Council, a select group of union representatives voted to confirm Elba Ester Gordillo in her position as union leader indefinitely, effectively making her SNTE president-for-life. During

Mexico's 2006 presidential election Gordillo formed her own political party and tacitly supported the candidacy of National Action Party (PAN) candidate Felipe Calderon, a critical factor in Calderon's ultimate electoral victory. Labor and political observers we have spoken with claim that the GOM's acquiescence on Gordillo's lifetime position is part of the PAN's payoff for Gordillo's political support in last year's presidential election. (Comment: Gordillo, who is often referred nationally as "the Teacher" is generally considered to be much more interested in increasing her personal wealth and political influence than she is in improving the quality of Mexico's corrupt and poorly performing public education system)

Gas Infrastructure "Recovering" After Attack

17. (SBU) Our sources remain confident that despite the damage to the Pemex Gas pipeline system by the July 5 and 10 EPR bombings of valve sites which affected several manufacturing sites in the states of Guanajuato and Queretaro, economic disruption will be minor. Bypass operations are currently underway and gas flows should restart by July 13. Less certain is the long term effect the attacks will have on investment (see septel).

Washington Governor Talks Apples, Trucking with Economia

18. (SBU) Washington State Governor Christine Gregoire raised the twelve-year litigation over tariffs on Washington State Red and Golden Delicious apples with Economy Secretariat Undersecretary of International Trade Negotiations Beatriz Leycegui. Leycegui offered to "look into the merits of the

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case" and asked what Washington State might be willing to "offer" to settle the dispute. Leycegui also asked Gregoire to encourage Washington State legislators to support the Cross Border Trucking Demonstration Project. She added that as a result of congressional delays on trucking, some groups in Mexico are questioning the need for Mexico to fulfill its own NAFTA commitments and are pressuring the GOM to take the next legal step with the U.S., i.e., a suspension of NAFTA benefits enjoyed by the U.S. Leycegui said she wanted to see better integration of Mexican and American markets and reduce the number of U.S.-Mexico bilateral trade disputes.

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